

DRAFT

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA
ENERGY DIVISION
I. D. #5451
RESOLUTION E-3981
May 25, 2006

R E S O L U T I O N

Resolution E-3981. Southern California Edison (SCE) requests confirmation that costs incurred by SCE pursuant to a standstill agreement entered into with Peabody Western Coal Company (Peabody) and the Black Mesa Pipeline Company are fuel-related costs that can be recorded directly into the Energy Resource Recovery Account (ERRA) balancing account.

By Advice Letter 1952-E Filed on December 29, 2005.

SUMMARY

SCE may record \$5.013 million in standstill agreement costs to the ERRA balancing account.

This Resolution confirms Energy Division's concurrence with Southern California Edison (SCE) that recording standstill agreement costs to the ERRA balancing account is appropriate.

SCE should be prepared to demonstrate that it exercised reasonable due diligence and negotiated in good faith to modify the pollution control requirements in order to recover the standstill agreement cost in rates.

BACKGROUND

SCE was in discussion to maintain its coal fuel supply while efforts were made to reopen Mohave.

On December 31, 2005, Mohave Generating Station (Mohave) a two-unit, coal fired power plant located in Laughlin, Nevada, shut down operations. Mohave's coal supply contract with Peabody also expired at the end of 2005.

SCE was negotiating to preserve the option for continued coal operations at Mohave, prior to installation of pollution control equipment. In conjunction with that effort, SCE was in discussions with Peabody for a temporary agreement in which Peabody would maintain the Black Mesa Mine in sufficient readiness so as to permit a timely return to production if SCE's effort for continued coal operations of Mohave was successful.

SCE plans to record standstill agreement costs directly to the ERRA balancing account.

SCE believes that recording the standstill agreement costs directly to the ERRA balancing account is appropriate since this ratemaking treatment is consistent with SCE's currently effective Commission-approved ERRA tariff which authorizes Utility Retained Generation (URG) Fuel and Fuel-related Expenses to be recorded in the ERRA balancing account as they are incurred.

SCE's URG Fuel and Fuel-related Expenses are defined in SCE's ERRA tariff as: (1) variable fuel expenses (commodity and fuel transportation), (2) fixed (unavoidable) fuel expenses, (3) fuel inventory carrying charges, (4) fuel contract settlement, buy-out, and renegotiation costs, and (5) other costs as approved by the Commission.

The standstill arrangement is similar to the activities contemplated in the ERRA forecast proceeding.

SCE believes that these activities are analogous to the activities contemplated in SCE's 2006 ERRA forecast of operations proceeding (A.05-08-002). While that forecast assumed that Mohave would be temporarily shut down during 2006, SCE identified costs necessary to maintain or preserve the Black Mesa Mine coal supply. No party opposed SCE's ERRA proceeding revenue requirement. The standstill arrangement is similar to the activities contemplated in the ERRA forecast.

Standstill agreement costs will be subject to reasonableness review.

Like any other fuel-related costs recorded in the ERRA balancing account, SCE's actual fuel-related standstill agreement costs will be subject to full review by the Commission and other interested parties in SCE's annual ERRA reasonableness of operations proceeding.

SCE seeks confirmation that Energy Division concurs in its treatment of the standstill agreement costs.

SCE is filing AL 1952-E to clarify that costs that SCE may incur according to a standstill agreement are fuel-related costs that can be recorded directly to the ERRRA balancing account.

NOTICE

Notice of AL 1952-E was made by publication in the Commission's Daily Calendar. SCE states that a copy of the Advice Letter was mailed and distributed in accordance with Section III-G of General Order 96-A.

PROTESTS

Advice Letter AL 1952-E was protested.

SCE's Advice Letter AL 1952-E was timely protested by The Natural Resources Defense Council (NRDC) on January 18, 2006.

NRDC protests that SCE did not recognize, and request funding for, generation alternatives to Mohave

NRDC filed protests to AL 1952-E, and AL 1953-E (also related to Mohave) in the same letter. NRDC protests that SCE's advice letters do not recognize generation alternatives to Mohave and that SCE should request funds to pursue development of the alternatives identified in a forthcoming final study. NRDC also suggests that the CPUC should be mindful of the long-term effects associated with greenhouse gas emissions that are associated with a return to operation of Mohave.

SCE responded to NRDC's protest on January 25, 2006.

SCE's response to NRDC's protest is discussed in Resolution E-3977 for AL 1953-E.

NRDC's protest does not relate to SCE recording standstill agreement costs to the ERRRA balancing account, the subject of AL 1952-E, and this Resolution. NRDC's

protest concern general issues surrounding continued Mohave operations. SCE's response to NRDC's protest is addressed in Resolution E-3977 for AL 1953-E.

DISCUSSION

Energy Division agrees that recording standstill agreement cost to the ERRA balancing account while SCE negotiated to reopen Mohave is appropriate. SCE may record standstill agreement cost of \$5,013,361 in the ERRA.

ERRA balancing account records URG fuel and fuel-related expenses.

Decision 02-10-062 established the ERRA balancing account. The purpose of the ERRA is, among other things, to record SCE's URG fuel costs. URG includes all of SCE's generating facilities, including its ownership share of Mohave. SCE's URG fuel and fuel-related expenses include:

- Variable fuel expenses (commodity and fuel transportation);
- Fixed (unavoidable) fuel expenses;
- Fuel inventory carry charges;
- Fuel contract settlement, buyout, and renegotiation costs;
- And other costs as approved by the Commission.

The standstill agreement cost is fuel-related.

On December 31, 2005, SCE shut down operations at Mohave due to emission control requirements. SCE's coal fuel contract with Peabody also terminated on that date. While negotiating to resume operations at Mohave prior to installation of pollution control equipments, SCE entered into a standstill agreement with Peabody to preserve its coal fuel supply. The standstill agreement was not extended beyond its termination date of March 31, 2006.

The standstill agreement cost is fuel-related. As such, it is appropriate to record the standstill agreement costs in the ERRA balancing account.

Mohave standstill agreement fuel-related expenses recorded to the ERRA balancing account is capped at \$5.013 million.

Resumption of operation at Mohave is uncertain. In its March 29, 2006 monthly Mohave status report, SCE concluded that further aggressive pursuit of interim

operations at this time was not warranted, and SCE's current estimate was that Mohave will not resume operating before approximately 2010.

Additionally, the standstill agreement which was entered into in late December 2005 has not been extended beyond its termination date of March 31, 2006.

As such, SCE may record in the ERRA balancing account, \$5,013,361 which represents SCE's 56% share of standstill agreement costs (including royalties and taxes) entered into with Peabody as of December 29, 2005.

Recovery of standstill agreement costs is subject to Commission review in SCE's annual ERRA reasonableness of operations proceeding.

Standstill agreement costs recorded in the ERRA will be subject to a reasonableness review before SCE can recover the recorded costs. SCE should request recovery in its annual ERRA reasonableness of operations proceeding.

SCE must demonstrate that the standstill agreement costs were reasonably incurred.

In its application to justify recovery in rates of standstill agreement costs, SCE should be prepared to demonstrate that, while the standstill agreement was in effect, SCE exercised reasonable due diligence and negotiated in good faith to modify the pollution control requirements. SCE's demonstrations should include, at a minimum, renegotiation meeting agendas, minutes, and change in term proposals.

NRDC's protest is not related to standstill agreement costs.

NRDC filed its protest to AL 1952-E and AL 1953-E in the same letter. NRDC's protest does not address the specific question of whether the standstill agreement costs should be recorded to the ERRA balancing account. As noted in Resolution E-3977-E to AL 1953-E, NRDC's concerns and comments may be better addressed in future Mohave proceedings that are broader in scope. NRDC's protest is denied.

COMMENTS

Public Utilities Code section 311(g)(1) provides that this resolution must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission.

The 30-day comment period for the draft of this resolution was neither waived or reduced. Accordingly, this draft resolution was mailed to parties for comments. This draft resolution will be placed on the Commission's agenda for the May 11, 2006 meeting.

No parties submitted comments.

FINDINGS

1. D.02-10-062 established the Energy Resource Recovery Account (ERRA) balancing account.
2. The purpose of the ERRA is, among other things, to record SCE's Utility Retained Generation (URG) fuel costs.
3. URG includes all of SCE's generating facilities, including its ownership share of Mohave.
4. SCE URG fuel and fuel-related expenses include:
 - Variable fuel expenses (commodity and fuel transportation);
 - Fixed (unavoidable) fuel expenses;
 - Fuel inventory carry charges;
 - Fuel contract settlement, buyout, and renegotiation costs;
 - And other costs as approved by the Commission.
5. SCE shut down operations at Mohave on December 31, 2005.
6. SCE's coal fuel supply contract with Peabody Western Coal Company (Peabody) terminated on December 31, 2005.
7. SCE entered into a standstill agreement with Peabody to preserve its coal fuel supply while negotiating to resume operations at Mohave.
8. SCE filed AL 1952-E on December 29, 2005 requesting authorization to record standstill agreement costs in the ERRA balancing account.
9. The Natural Resources Defense Council (NRDC) timely protested SCE's Advice Letter 1952-E on January 18, 2006.
10. SCE responded to NRDC on January 25, 2006.
11. The standstill agreement is fuel-related.

12. Energy Division concurs that it is appropriate to record the standstill agreement cost in the ERRA balancing account.
13. Resumption of operation at Mohave is uncertain.
14. In its March 29, 2006 monthly Mohave status report, SCE reported that further aggressive pursuit of interim operations at this time was not warranted, and that SCE's current estimate was that Mohave will not resume operating before approximately 2010.
15. SCE also reported that the standstill agreement has not been extended beyond its current termination date of March 31, 2006.
16. SCE's 56% share of standstill agreement cost (including royalties and taxes) is \$5,013,361.03.

THEREFORE IT IS ORDERED THAT:

1. The request of the Southern California Edison (SCE) for confirmation that the Energy Division concurs with SCE's recordation of standstill costs to the Energy Resource Recovery Account (ERRA) as requested in Advice Letter AL 1952-E is approved, as modified in Ordering Paragraph 3, 4, and 5.
2. Energy Division concurs with recording standstill agreement costs to the ERRA balancing account, subject to cost limitation.
3. SCE may record in the ERRA balancing account, SCE's 56% share of standstill agreement cost (including royalties and taxes) of \$5,013,361.03 entered into with Peabody as of December 29, 2005.
4. Recovery of standstill agreement cost is subject to Commission review in SCE's annual ERRA reasonableness of operations proceeding.
5. To recover standstill agreement costs in rates, SCE must demonstrate that, while the standstill agreement was in effect, SCE exercised reasonable due diligence and negotiated in good faith to modify the pollution control requirements.
6. The Natural Resources Defense Council's protest is denied.

This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on May 25, 2006; the following Commissioners voting favorably thereon:

STEVE LARSON
Executive Director